



Newsletter

SMEAD US VALUE — 3RD QUARTER 2026 (9/30/2026)

Breaking the Fever

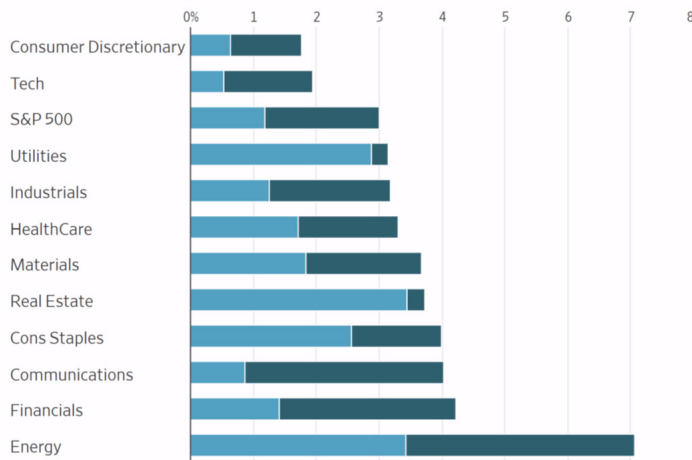
When I was a child, we were told, “Starve a cold and feed a fever.” This appears to us to be what is going on in the stock market as we enter the fourth quarter of 2026. A massive capital investment cycle needed to build out data centers and invest in the inputs needed to use artificial intelligence has fed a feverish demand for money. Simultaneously, the U.S. Federal government is running huge budget deficits. This follows a spectacular performance, with relatively short interruptions in a 17-year bull run for the S&P 500 Index. This produced an incredible compounded return of 1,463.9%.

Our long-time investors are very aware that back in 2020-2024, we were arguing that the historically low interest rates created in the COVID-19 debacle would eventually normalize. Welcome, everyone, to normalization. What investors are not doing is adjusting the prices of common stocks based on discounting long-term net profits into today's dollars at the newly and much higher rates!

You see, “a bird in the hand is worth two in the bush.” Therefore, as interest rates rise, you should naturally want to receive compensation for your risk sooner rather than later. We are leaning into the industries that have higher owner earnings and free cash flows now and avoiding the industries that intend to provide the returns farthest out into the future.

Total cash yield in 2025

■ Dividend yield ■ Buyback yield

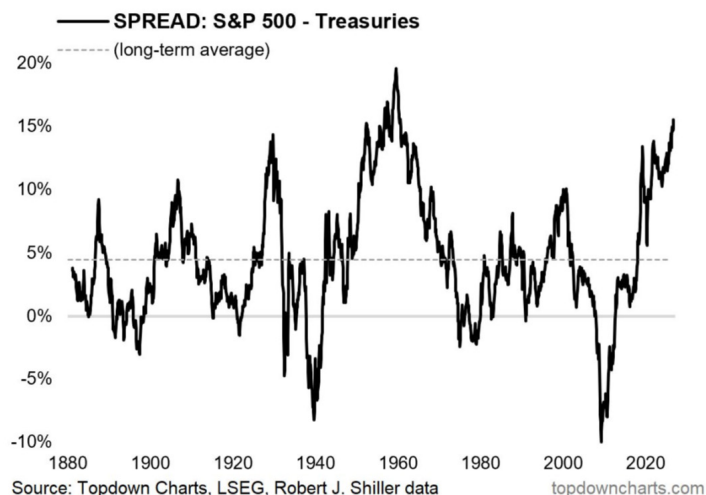


Source: S&P Dow Jones Indices

There are limits to how far the stock market can go in its excitement for euphoric circumstances. Prior maniacal markets peaked at around 40% concentration in the hot area of the S&P 500 Index. We happen to be there now. As we were prone to say back in the 1980s and 1990s, “If the Generals are leading and the troops are not following, the Generals will get slaughtered in the battle!” In the month of September, 70% of the stocks in the S&P 500 fell. The index gained 0.36% as the Generals continued marching forward.

This leads us to the questions, what usually breaks the fever, and which common stocks might benefit from it breaking? Barry Bannister, from Stifel, is one of our favorite information providers and he provided a chart that might answer the question.

Rolling 10-Year Total Returns: Stocks vs Bonds



Breaking the Fever

Interest rate sensitive stocks like homebuilders would be a beneficiary of breaking the fever as mortgage rates should come down. Other charts we've seen argue that when oil outperforms gold, value investing strongly outperforms growth! We are seeing this in real time.

In conclusion, we are more than willing to bypass whatever remaining gains are to be had from the continuation of the current euphoric and maniacal phase in stocks to defend against losing money. As Warren Buffett would say, rule number one is never lose money, and rule number two is never forget rule number one. We are excited to see how markets adjust when the fever breaks.

Play the long game,



Bill Smead
Lead Portfolio Manager



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Co-Portfolio Manager



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